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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
2000 Biennial Regulatory Review	)	**CC Docket No. 00-199**
Comprehensive Review of the Accounting	)	
Requirements and ARMIS Reporting	)	
Requirements for Incumbent Local Exchange	)	
Carriers: Phase 2 and Phase 3	)	

WORLDCOM PHASE III REPLY COMMENTS

State commissions and other non-ILEC commenters agree that it is premature for the Commission to adopt specific "triggers" that would permit the ILECs to escape the Part 32 or Part 64 accounting rules.[1]

The ILECs, on the other hand, take the extreme position the Commission should eliminate its accounting rules under existing competitive and regulatory conditions. They suggest that GAAP accounting and SEC reporting, supplemented by special studies on an "as needed" basis, would be sufficient to meet the regulatory needs of the Commission and the states. Indeed, they suggest that the Commission's accounting rules are a historical artifact and would not be adopted today if the Commission were working from a blank slate.[2]

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[1]See, e.g., Wisconsin Comments at 3.

[2]See, e.g., Verizon Comments at 2.

As an initial matter, any review of the Commission's accounting rules must recognize that the Commission and the states are <u>not</u> working from a blank slate. Reflecting their statutory obligations, the Commission and state regulators have designed a variety of regulatory mechanisms that explicitly make use of the results produced by the Part 32 and Part 64 accounting rules. Given that the accounting rules are the foundation for these regulatory mechanisms, the Commission cannot evaluate its accounting rules in isolation from its other rules.

The most obvious example of a regulatory mechanism that relies on the results produced by the Part 32 and Part 64 accounting rules is the Part 36 separations process. Even if the Commission elects to adopt the proposed freeze of separations allocators, the separations process will start with the Part 32 account structure. While it is perhaps conceivable that the Commission and the states could design a separations system that was not based on the Part 32 account structure, as Verizon suggests,[3] such an approach is wholly impractical at this time. To date, no party has even proposed to the Separations Joint Board that it explore the creation of a separations system that is not based on the Part 32 account structure.

More generally, non-ILEC commenters agree that the Commission's review of its accounting rules must recognize that the USOA is used not only by the Commission but by the states as well. As GSA explains, "[s]ince only the Commission is in a position to require

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[3]Verizon Comments at 5.

uniformity of accounting and reporting throughout the nation, the Commission must consider both Federal and state regulatory needs in assessing changes to its rules."[4]

With respect to the Commission's responsibilities, Verizon is simply incorrect when it contends that "[t]he Commission no longer has a regulatory need to identify interstate costs if a carrier cannot take advantage of the lower formula adjustment."[5] As long as an ILEC remains dominant, comprehensive and consistent reporting of interstate costs is required in order to permit the Commission and ILEC customers assess the reasonableness of ILEC rates and, consequently, determine whether to conduct an investigation pursuant to Section 204 or 205 or file a complaint pursuant to Section 208.

In at least five respects, SEC reports based on GAAP would fall short of providing the necessary comprehensive and consistent cost data.

- SEC financial reports do not allow the Commission or the ILECs' customers to distinguish between the ILECs' regulated and nonregulated operations, or to distinguish between the ILECs' dominant local operations and their nondominant interLATA operations. The ILECs' parent companies are diversified corporations whose reported financial results are not sufficiently disaggregated to permit the Commission to obtain information concerning their dominant carrier operations.
- As discussed above, SEC reports based on GAAP would not permit the Commission to distinguish interstate from intrastate costs.

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[4]GSA Comments at 4.

[5]Verizon Comments at 5.

- GAAP alone does not ensure consistency and uniformity in ILEC accounting practices. For example, as the Commission discussed in the GAAP Order, "the GAAP definition of materiality leaves too much to the discretion of parties not bound by our public interest responsibilities to be viable in a regulatory accounting scheme."[6] This lack of consistency would impair the Commission's ability to monitor ILEC performance using benchmarking.
- As the Commission has recently confirmed, GAAP does not prevent the ILECs from booking excessive depreciation expense.[7] Consistent and reasonable depreciation practices are particularly significant in a capital-intensive industry such as telecommunications.
- SEC reports provide no detail concerning the costs associated with different network components, e.g.., they do not distinguish loop costs from other costs. This level of detail continues to be relevant in assessing the reasonableness of rates charged for particular interstate rate elements. The lack of detail in SEC reports concerning the embedded costs of particular network components or overhead functions would also impair the Commission's ability to evaluate forward-looking cost studies related to interconnection and universal service.[8]

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[6]Revision of the Uniform System of Accounts for Telephone Companies to Accommodate Generally Accepted Accounting Principles, Report and Order, 102 FCC 2d 964, 986 (1985).

[7]In the Matter of 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, Report and Order, 15 FCC Rcd 242, ¶ 42 (1999).

[8]See, e.g., AT&T Comments at 2; Wisconsin Comments at 3-4.

In light of the fact that SEC reports based on GAAP do not provide the requisite comprehensive and consistent financial information concerning the ILECs' dominant carrier operations, the Commission should make clear that it will not make significant "Phase III" modifications to the core requirements of Part 32 or Part 64 before there is clear evidence that an ILEC is operating in a robustly competitive local exchange and exchange access market.

Contrary to the ILECs' claim, the Part 32 rules do not in any way "distort" the market. As an initial matter, the regulatory burden associated with the Part 32 rules is minuscule.[9] More importantly, the ILECs refuse to acknowledge that they are subject to the Part 32 rules only because they are dominant carriers. Whatever "burdens" are imposed by the Part 32 rules, they pale in comparison to the benefits of incumbency. And whatever "distortion" of the market may result from the Part 32 rules pales in comparison to the distortion of the market that results from the dominant carriers' control of bottleneck facilities.

Respectfully submitted,
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March 14, 2001

[9]In a 1998 report prepared for the ILECs, Arthur Andersen estimated that Part 32 imposed additional costs of approximately $2 million per year on each large ILEC. CC Docket No. 98-81, July 15, 1998, at 20.

STATEMENT OF VERIFICATION

I have read the foregoing, and to the best of my knowledge, information, and belief there is good ground to support it, and that it is not interposed for delay. I verify under penalty of perjury that the foregoing is true and correct. Executed on March 14, 2001.

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CERTIFICATE OF SERVICE

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